Mathias Larsen James Jackson December 10th, 2025

While Western central banks hesitate on climate, China's acts

Of the four largest central banks, three have failed to turn climate rhetoric into action. The Federal Reserve has chosen abstention. The European Central Bank and the Bank of England have chosen cautious risk management. Only the People's Bank of China has chosen direct intervention. ***Mathias Larsen*** *and* ***James Jackson*** *analyse the four institutions' motivations and approaches.*

Climate change is no longer a distant problem. The physical changes to the global environment are a macroeconomic force reshaping inflation, financial stability and long-term growth. Central banks now routinely acknowledge this reality. But when it comes to action – rather than rhetoric – a stark divide has emerged between the world's four most powerful monetary authorities. As our new working paper sets out, all are analysing the problem, but only one of them acts.

America's Federal Reserve (the Fed) is the clearest case of institutional resistance. Its chair, Jerome Powell, has repeatedly drawn a hard line between climate policy and the work of the Fed. In early 2025 the Fed withdrew from the Network for Greening the Financial System (NGFS), a group of 148 central banks formed to contribute to the development of environmental and climate risk in the financial sector and to "mobilise mainstream finance to support the transition toward a sustainable economy." At a press conference two weeks later Mr Powell explained that the Fed "joined to get the benefit of understanding what other central banks were doing and seeing research," but later decided "that the activities of the NGFS are not a good fit for the Fed, given our current mandate and authority." He went on to pronounce that "Other central banks have different mandates and belong to the NGFS," and while he had no criticism of them it was "not right for the Fed."

This position has concrete consequences. While the Fed has conducted limited climate scenario analysis and issued supervisory guidance, but it has never adjusted interest rates, collateral rules or emergency lending programmes to reflect climate risk or support decarbonisation. During the covid-19 pandemic, the Fed's enormous asset purchases overwhelmingly favoured carbon-intensive sectors under the banner of "market neutrality." The Fed insists it is not a climate policymaker, but by preserving existing financial structures, it indirectly obstructs the needed economic transformation.

The European Central Bank (ECB) strikes a very different rhetorical tone. It remains a member of the NGFS (as do the other institutions on our list). And its President, Christine Lagarde, has placed climate at the heart of the institution's public narrative.

"If we do not account for the impact of climate change on our economy, we risk missing a crucial part of the overall picture. This means that our job of preserving price stability must include further work on better understanding how climate change affects our role. We must incorporate climate change into everything we do: our models, data, projections and analyses. Ultimately, we need to ensure that our monetary policy accounts for the impact of climate change."

The ECB has indeed been more active than the Fed in measurement and disclosure. It has run climate stress tests, integrated climate variables into risk modelling, adjusted its collateral framework and in 2022 briefly tilted its corporate bond purchases away from high-emitting firms. Yet the limits of this approach are now clear. The green bond tilt was modest in scale and was dropped in 2023. Core refinancing operations and interest-rate policy remain climate-neutral in practice. In July 2025 the bank proclaimed a green collateral policy, but with few details on its future magnitude. The ECB's climate policy focuses on managing risk, not on redirecting capital at the needed scale.

The Bank of England (BoE) once appeared ready to push further. Under Mark Carney, governor between 2013 and 2020, the Bank helped to elevate climate to a central banking issue globally. The BoE adopted climate stress testing, adjusted asset purchases and explicitly linked net-zero objectives to financial stability. In a speech in 2021 Mr Carney's successor, Andrew Bailey, declared, in language that mirrors the ECB:

"Risks to the economic outlook make climate change and the transition to a net-zero economy [are] also relevant factors for the conduct of monetary policy. The physical effects of climate change, such as rising sea levels and more frequent severe weather events, as well as the transition to a net-zero economy,through changes in government climate policy, technology and consumer preferences, create financial risks and economic consequences."

Yet the BoE's experiment in green central banking never scaled up to align with the rhetoric. The green tilt in asset purchases ended. Officials increasingly stressed that climate lay outside the Bank's "primary mandate." Like the ECB, the BoE treats climate largely as a supervisory concern rather than a monetary one.

Then there is the People's Bank of China (PBoC). Unlike Western central banks, the PBoC does not claim insulation from state priorities. It explicitly aligns its work with the country's national decarbonisation strategy. As Yi Gang, governor between 2018 and 2023, put it:

"We should study and implement [President] Xi Jinping's thought on ecological conservation in an earnest and profound manner, and make utmost efforts to peak carbon emissions before 2030 and achieve carbon neutrality before 2060 (the "30-60" decarbonisation goal)…In this process, we've managed to give full play to the decisive role of market in allocating resources and better leverage the role of government at the same time."

> *Unlike Western central banks, the PBoC does not claim insulation from state priorities. It explicitly aligns its work with the country's national decarbonisation strategy.*

This is not just political language. The PBoC has constructed the world's most developed system of green monetary instruments. Green loans and high-quality green bonds receive preferential treatment in key liquidity facilities. Banks' green performance influences their macroprudential assessments, influencing interest rates on required reserves. Most importantly, the PBoC operates a targeted Carbon Emission Reduction Facility that provides low-cost funding for banks financing renewables and clean technologies. Since 2021 this facility alone has supported well over $150 billion in green lending.

Independence vs government-directing

The contrast reflects not technological capacity but institutional philosophy. Western central banks operate under a doctrine of independence and depoliticisation that treats direct credit allocation as politically illegitimate. Climate change is acceptable so long as it appears as a risk variable, not as a justification for reshaping financial flows, even if doing so is a political priority of the country's government. The PBoC operates under a different model: the government sets strategic goals and the central bank designs the tools. We call this "government-directing with operational independence".

This arrangement has enabled China's central bank to use monetary power for structural transformation rather than passive observation. Western central banks, by contrast, continue to act as if steering capital is inherently more political than leaving markets to entrench fossil-heavy financing paths.

Rethinking central bank independence for the climate era

Central bank independence was established to solve the inflation crises of the late twentieth century. It was never designed to manage planetary instability. Climate change is not a marginal financial risk but a structural macroeconomic transformation. Treating it solely as a risk problem, seemingly, turns prudence into paralysis.

The verdict of comparison is unambiguous. The Fed has chosen abstention. The ECB and BoE have chosen cautious risk management. Only the PBoC has chosen direct intervention. Each reflects a different answer to a defining question of our age: is climate change someone else's responsibility, or is it a core task of central banks?

History will likely judge central banks less by their climate speeches than by what they actually financed. By that standard, only one of the world's four most powerful monetary authorities is acting as though the climate transition is a central banking problem. And it is, not coincidentally, the only one of the four that is not independent of the government.

This article gives the views of the author, not the position of LSE Business Review or the London School of Economics. You are agreeing with our comment policy when you leave a comment.

Image credit: humphery provided by Shutterstock

About the author

Mathias Larsen

Mathias Larsen is a Senior Policy Fellow at the Global School of Sustainability at LSE where he leads the work on China. His work focuses on assisting policymakers in China in advancing the country's green transition, as well as supporting policymakers in other countries as they respond to China's role in a global green transition.

James Jackson

James Jackson is a Hallsworth Research Fellow at the Sustainable Consumption Institute and Department of Politics at the University of Manchester. His research is focused on the political economy of climate change, particularly the intersection of fiscal, monetary and climate policy.

Posted In: Economics and Finance | LSE Comment | Sustainability